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U.S. Approach to Problems in the Caribbean Basin

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Following is a statement by Secretary Shultz before the Senate Committee on Finance, August 2, 1982.

We all know we live in a troubled world. We also know that the United States as a great nation must face up to these troubles and do its part to try to resolve them. I am here to testify today about an innovative and creative program which this Administration is proposing to address the problems of our immediate neighbors to the south—the Caribbean Basin.

The security and well-being of the countries of the Caribbean and Central America are vital to the United States and to the Western Hemisphere as a whole. Their crisis today is many sided and involves both emergency and long-term problems. Our response is comprehensive and integrated with regard to the problems and needs of individual countries and also with regard to the contributions they and their other neighbors—Canada, Colombia, Mexico, and Venezuela—can make to resolve their problems. The President's Caribbean Basin Initiative is an outstanding example of the steadiness and seriousness with which we view our relations with the other countries of the Americas.

Urgent Need for the Initiative

When I learned of the President's initiative, I was in the private sector. At the time, I thought it was the right medicine. Since then I have seen that the problems are even more severe than I imagined. The program is not just good medicine; it is vital.

We are talking about an area which is of crucial and immediate concern to our own self-interest. You need only glance at a map to see that it is indeed our third border. If this area should be dominated by regimes hostile to us or if it becomes the scene of prolonged social upheavals, the impact on our own economy and society would, indeed, be of major proportions. Let me give just a few examples of how closely we are linked with the basin countries.

First, the sea lanes of the Caribbean are a lifeline of our trade—one-half of all our imports and exports pass through this region, including three-quarters of our oil imports.

Second, many of our people have roots in the area. One out of five people alive today who were born in Barbados live in the United States; the same is true for one out of six Jamaicans, and one out of ten Salvadorans.

Third, given proximity and existing ties, the United States is a natural safehaven for those fleeing social and economic pressures in the basin. These pressures create illegal immigration, itself a great problem for us. The basin area is now the second largest place of origin of illegal immigration.

Fourth, the Caribbean is now a $7 billion market.

Clearly then, we have an enormous stake in helping our neighbors achieve economic and political stability.

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When President Reagan announced this program on February 24 before the Organization of American States, and when he transmitted this legislation to the Congress on March 17, he stressed that there is an economic crisis in the Caribbean Basin that threatened our own well-being and the peace and prosperity of the whole hemisphere. That crisis has not gone away. In fact, it has deepened. These small countries to our south are acutely vulnerable to developments in the world economy. Over the last few years they have seen dramatic reversals in their terms of trade, as their oil and other imports have increased in price and their traditional exports have fallen in price. The worldwide slowdown in economic growth has choked off opportunities for developing new types of exports to the world market, as well as cut into tourism which has been an important source of foreign exchange for them.

As a result they are not able to earn enough foreign exchange to pay for the imports they need. The productive base in these countries, already inadequate to provide the jobs and products which their populations need, is being eroded by acute shortages of spare parts and by the lack of raw materials and agricultural inputs. The result is a rise in unemployment and underemployment which is of truly major proportions—25% to 40% in many countries. Added to the evils of inflation, spiraling foreign debt, and major balance-of-payments problems, it amounts to an almost classic recipe for social discontent and loss of confidence in the future.

This is the kind of environment upon which the extreme and violent minorities on both sides of the political spectrum can feed and produce major political and social upheavals. It is an extraordinary tribute to the strength of democratic and humane traditions in the region that the vast majority of countries in the area are governed by democratically elected governments. In the last 5 months, since the time that the President announced the program on February 24, elections have been held and new democratic governments chosen in six countries. Many of the countries in this region have strong new leadership which is committed to adjusting the structure of their economies to reflect the hard new economic realities which they face. The Caribbean Basin Initiative is aimed at helping these countries to implement the painful but unavoidable reforms which can reverse the deterioration and lead to self-sustaining growth. Its purpose is to help restore the faith of their peoples in their countries' ability to provide them with a better future.

Integration of Economic Programs

The program which the Administration has proposed to the Congress for the Caribbean Basin addresses the enormous economic problems in the area in a comprehensive way. It is an innovative program in several ways.

First, it integrates three types of economic programs—trade opportunities, investment incentives, and aid. Each of these elements provides significant benefits. Even more importantly, each element reinforces the other. The emergency financial assistance will help countries cope with their short-term balance-of-payments and liquidity problems. The one-way free trade area and the investment tax credit will give long-term incentives for new investment to promote self-sustaining growth. The program as a whole is greater than the sum of its parts. We need to maintain the integrity of each element to insure the effectiveness of the program as a whole.

Second, this program is part of a major multilateral effort, particularly by Canada, Colombia, Mexico, and Venezuela. These four countries have already implemented improved programs of financial and technical assistance, as well as expanded new trade opportunities to the countries of this region. Their effort is impressive. It is particularly impressive since three of these countries are still developing countries themselves. Their effort is based on the perception—which we all share—that we cannot ignore the events in our neighborhood and that—to insure our own long-term prosperity and stability—we must assist our neighbors to achieve the same goals themselves.

Third, this program was developed out of a continuing process of consultations with the countries in the region. It reflects their own priorities and assessments of their particular needs, as well as their own efforts and programs. It is thus very much a cooperative program and not a unilateral plan imposed by Washington.

The program was also developed in close cooperation with Puerto Rico and the Virgin Islands and includes important features to assure that the territories share fully in the renewed economic growth in the region. For this reason I am deeply concerned about the potential impact on the territories of the curtailment of tax benefits recently adopted by this committee.

Trade and Investment Provisions

Let me spend just a few minutes on the trade and investment provisions in the legislation since these aspects are of particular interest to the committee. We already provide liberal entry into our market for much of the trade from basin countries. But there are several important limitations. First, some of the duties which remain in place are in sectors of special interest to the basin countries. And in other cases the duties which remain in place limit expansion into new and nontraditional export products. Second, a large part of the basin's present duty-free entry into our market comes from the generalized system of preferences (GSP). However, the GSP has ceilings on duty-free benefits, as well as product exclusions; these were established in the program largely for global reasons that are not relevant to the Caribbean Basin. These limitations, and the whole complex structure of the GSP, limits the ability of small and relatively inexperienced traders—which is often the case for the Caribbean Basin—to take advantage of the GSP opportunities.

The Administration's proposal asks for duty-free treatment for all products from the basin except textiles and apparel. The proposal includes safeguards to provide relief to any U.S. industry seriously injured by increased basin imports. There are also provisions to protect the U.S. domestic sugar price support program where necessary. The proposal also includes a requirement for minimum local content to insure that the free trade area does not encourage mere "pass-through" operations involving little value added in the basin countries.

This proposal is a carefully balanced package which provides major benefits to the Caribbean Basin countries but also safeguards essential U.S. economic interests. It is dramatic and simple. While the economic benefits of the free-trade area are long term, the offer of an unimpeded U.S. market to those small nations is a major political commitment with immediate impact. It will strongly encourage sound internal economic policies in order to take full advantage of this offer. This proposal relies on the market and not on artificial incentives. It eliminates duty barriers to our market, and thus it allows the enormous size of the U.S. market in itself to provide enormous and continuing incentives for investment, innovation, and risk taking in the Caribbean Basin.

The Administration is also proposing extension of the domestic tax credit to the Caribbean Basin. U.S. investors would receive a credit up to 10% of the amount of new fixed asset investment in the basin countries. The system would operate in much the same fashion as does the credit granted domestically. We would grant this benefit for a 5-year

period to countries which enter into executive agreements with the United States for tax administration purposes.

This incentive, particularly when combined with the free-trade proposal, should have an important impact on U.S. investors' perceptions about the Caribbean Basin. In some cases the risks of investment in the basin have been perceived as high, especially when coupled with the startup costs of developing new markets and marketing channels, training new local employees and managers, and overcoming transportation bottlenecks. The tax incentive promises a better return to U.S. business which undertakes investment in the basin and thus should increase investment there.

I know that there is some concern that these proposals will damage production and employment opportunities in the United States. I can understand that concern, particularly given the period of slow economic growth and budget austerity through which we are passing at present. But I believe these concerns are exaggerated. First, we are such a big economy compared to those of the Caribbean Basin that what looms large in the basin will still have a small impact here. The combined gross national product (GNP) of all of the Caribbean Basin countries amounts to less than 2% of our GNP. Our imports from the Caribbean Basin account for less than 4% of our total imports worldwide. The imports that would be affected by our free-trade proposal are at present less than one-half of 1% of our total imports—or two-hundreths of 1% (.0002) of our GNP. I really do not expect that this region will have a serious negative impact on our producers and workers even if imports from that region should grow at explosive rates. Nevertheless, as I noted before, we have proposed in the legislation certain safeguard provisions to deal with those cases where serious injury might occur or might be threatened.

Second, I also want to emphasize that the long-term benefits of this initiative are far greater than the short-term costs. The region already buys nearly $7 billion of goods from the United States. A stable, democratic, and prosperous Caribbean Basin means a much larger and growing market for our exports and consequently significantly greater job opportunities for our workers.

Conclusion

I appreciate that the legislation we have proposed is complex and controversial. I appreciate that the legislative process on such a bill is necessarily time consuming and complicated. I also appreciate that the Congress is carrying a heavy burden of important, indeed urgent, legislative work. Nevertheless, I urge that this piece of legislation be given priority attention. The needs of the Caribbean Basin are urgent. The United States has an opportunity to play a constructive role in helping these countries shape a better future. That opportunity is there now, but it will not be there forever. We cannot afford to wait. We have already waited too long.

Our security and our credibility are at stake. The tragic war in the South Atlantic has led some hemispheric friends—mistakenly I believe—to challenge our commitment to them as a partner. We must show them this is not so. We must do our part. If we do not, the problems will escalate, not only in the Caribbean Basin but elsewhere in the hemisphere as well.

I ask for your own strong leadership, as well as the leadership and commitment of all the distinguished members of this committee, to insure rapid passage of this program. ■

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